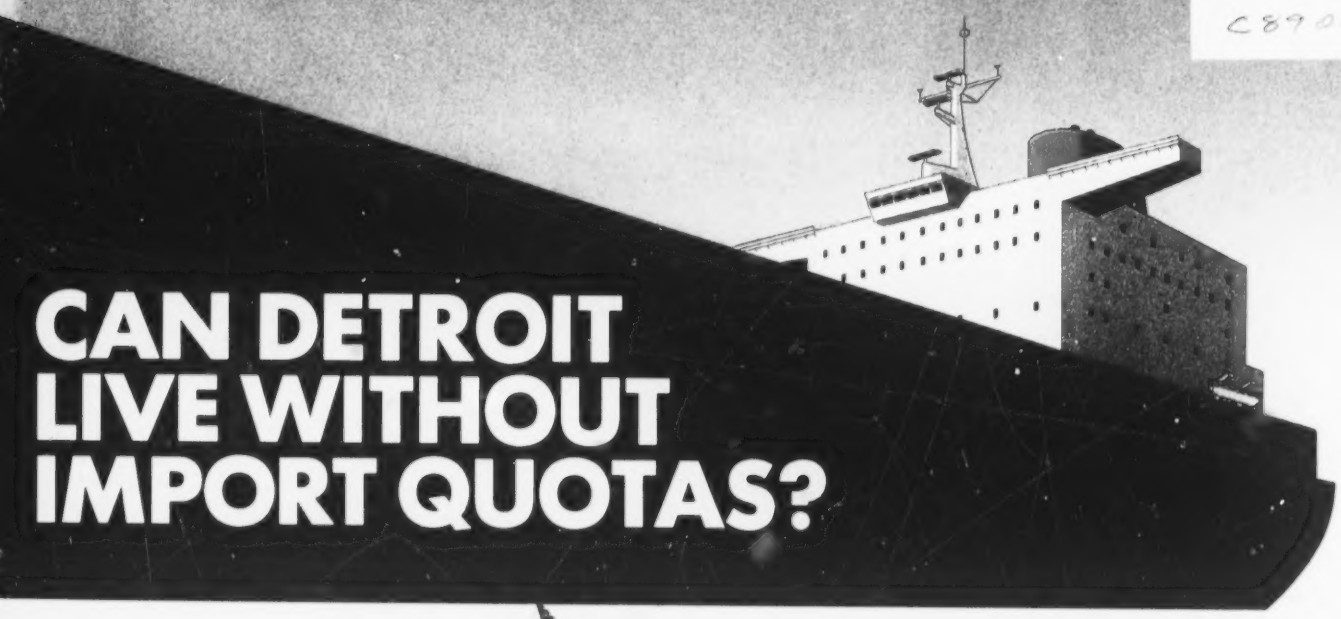
JUNE 25, 1984

$3.00

FORTUNE

5/12/84
C8900-1



CAN DETROIT LIVE WITHOUT IMPORT QUOTAS?

MANIPULATING PROFITS:

- HOW MANAGERS DO IT
- THE SPECIAL CASE OF AMERICAN EXPRESS

WHAT IF MONDALE WINS AFTER ALL

TURMOIL AT THE READER'S DIGEST

**********5-DIGIT 20814
MAY88 000 ES520099Y 52 08 1
CONGRSSNL INFO SVC MD00
4520 EAST-WEST HWY
STE 800
BETHESDA MD 20814

D 10093
724434

JUNE 25, 1984 VOL. 109, NO. 13

FORTUNE

Technology

If Washington lifts the gate and allows foreign cars to roll freely into the U.S., Detroit should still prosper. The reasons are examined in the story on page 20.

COMPETITION

Can Detroit Live Without Quotas? 20
Yes. Here's how. *by Anne B. Fisher*

THE ECONOMY

Fortune Forecast: Why Interest Rates Will Keep On Soaring 26
Two Wall Street economists blame a mismatch of saving and investment.

CORPORATE PERFORMANCE

Japan's Two-Fisted Telephone Maker 30
NEC thinks it can do one thing better than AT&T or IBM. *by Lee Smith*

Allegheny Ludlum Has Steel Figured Out 40
The productivity fanatic stayed profitable through the recession and is coining money now. *by Bill Saporito*

When Computers Chat, They Rely on Hayes 48

Kimberly-Clark Takes Off 48

MANAGING

Manipulating Profits: How It's Done 50
The rules leave ample room to fudge the numbers. *by Ford S. Worthy*

The Earnings Magic at American Express 58
"Special items" kept insurance profits on the rise. *by Carol J. Loomis*

Intrigue Behind the Ivy at Reader's Digest 64
Authority has moved into unlikely hands. *by Roy Rowan*

SELLING

Sears' Humbled Trading Empire 71
The retailer tried to imitate the Japanese trading companies, but couldn't learn the language. *by John W. Dizard*

Betting on a Beer Without Buzz 76

TECHNOLOGY

A Friendly Frontier for Female Pioneers 78
They're getting rich running software companies. (*A picture portfolio*)

A Start-up's Computer Is Wowing Engineers 89

MONEY & MARKETS

Scramble for Capital at Almost-Public Companies 91

A Testing Time for Adjustable Preferred 92

The Top Life Insurers Weigh Going Public 96

POLITICS & POLICY

What If Mondale Wins After All 98
He says he expects even business to like him. *by Anna Cifelli*

Unitary Taxes: A War on Sticky-Fingered States 113

Business Bets on the Congressional Races 113

A Yen Unfulfilled 114

PROFILE

The Curmudgeon Who Talks Tough on Quality 118
W. Edwards Deming brings his methods home to the U.S. *by Jeremy Main*

People to Watch 122

The Editor's Desk 4

News/Trends 8
Continental aftermath, regulating banks, distress investing, product liability, Phibro's rift, and more.

Follow-Up 11
Renewed doubts about formaldehyde, Beatrice's appetite, trendy K mart, Sotheby's on the rebound.

Letters to Fortune 15

Keeping Up 125
by Daniel Seligman

Personal Investing 129
Natural-resource mutual funds. Square D. Short-term securities. Portfolio Talk: Dennis Sherva of Morgan Stanley.
by John J. Curran

On the Road 137
High cuisine in low Manhattan.
by Walter McQuade

Books & Ideas 141
The trials of Mary and Bill.
by Michael Kinsley

Office Hours 147
Beating the clock.
by Walter Kiechel III

HARD TO SELL, DISTRESSED AND OTHER REAL ESTATE ACCEPTED BY RELIGIOUS CORPORATION. WILL STRUCTURE CONTRIBUTION OF REAL ESTATE TO MEET NEED OF DONOR.

IN UNITED STATES, CALL:

(516) 751-6644

SUPPORT THE HOME TEAM.

Buy An Olympic Coin.

For the first time in history, the United States Mint is issuing Olympic commemorative coins. Each beautiful gold and silver coin depicts an Olympic theme in honor of the first Summer Olympics held on American soil in over 50 years, the XXIII Olympiad in Los Angeles.

Coins can be purchased through your local post office and at participating banks and coin dealers across the country. Or, write to: U.S. Mint, Olympic Coin Program, P.O. Box 6766, San Francisco, CA 94101.

• • I.M.L.A. Olympic Organizing Committee M-1

THE TOP LIFE INSURERS WEIGH GOING PUBLIC

If mutual companies venture out of their cocoons, the upheaval—and Wall Street's take—could be enormous.

WALL STREET can be excused these days for drooling in anticipation of a potential feast. The nation's biggest life insurers—including such giants as Prudential, Metropolitan, and Equitable—are all seriously studying the possibility of converting from policyholder to stock ownership. Demutualization, as it's known in the trade, could produce some huge public offerings. The nation's top ten mutuals could have as much as $18 billion to distribute to existing policyholders in cash and stock, and they might want to raise billions in new capital.

While demutualization has looked appealing for some time, the Stark-Moore bill now before Congress has lately made the change a lot more compelling. According to most estimates, the bill would tax mutuals at a higher rate than stock companies. That's reason enough for the New York-based mutuals to rally around state legislation to legalize changeovers; only half the states permit it. Tax considerations are much on the mind of C.E.O. John J. Creedon of New York-based Metropolitan. "If Metropolitan has to pay $150 million a year more or $2.5 billion over the decade," he asks, "can you afford to give your competition that kind of edge?"

The only big mutual to decide on the switch so far is Union Mutual of Portland, Maine (assets: $4 billion), and tax savings are not its primary motivation. President Colin C. Hampton says he wants to tap the public marketplace for capital to finance acquisitions and the introduction of new products; he'd also be able to attract executives with stock options. Says Hampton: "We'll have more flexibility as a stock company."

Making the transition is a complex operation that could take Union a year. One of its toughest jobs is to figure the fairest way to divide up the pie among some 250,000 policyholders without giving away so much cash that the company jeopardizes its viability. Union must win approval of its plan from two-thirds of the policyholders.

Already some Wall Street houses are tackling another major problem: how to appraise the potential market value of a mutual turned stock company. Since mutual insurance companies use so-called statutory accounting methods, considered more conservative than generally accepted accounting principles, their "surplus"—analogous to shareholders' equity—understates their net worth. For example, they expense the selling cost of a new policy in one year rather than over the life of the policy. One way to make the figure comparable would be to write up the surplus by 50% to 100%. In Pru's case a 50% write-up would produce shareholders' equity of $4.5 billion.

Demutualization could discomfit some insurance company managements, putting them under public scrutiny and exposing their companies for the first time to takeovers. Still, most industry observers believe that competitive pressures from the big financial supermarkets will force the mutuals to enter the jungle. Declares James H. MacNaughton, a corporate finance expert at Salomon Brothers, "It's inevitable. If you're going to be good, you've got to have enough capital."

— Eleanor Johnson Tracy

The Ten Biggest Mutuals

Their surpluses, experts say, give a conservative idea of their book value as stock companies.

LIFE INSURANCE COMPANY	ASSETS in billions 12/31/83	SURPLUS in billions
Prudential	$72.2	$3.0
Metropolitan	$60.6	$2.5
Equitable	$43.3	$1.2
New York Life	$24.2	$1.4
John Hancock	$23.5	$1.0
Northwestern Mutual	$14.5	$.8
Massachusetts Mutual	$12.2	$.8
Bankers Life	$11.4	$.3
Mutual of New York	$9.3	$.5
New England Mutual	$8.5	$.5